DOCUMENT RESUME

ED 321 418 EA 022 096

TITLE Business Management Practices and Requirements for Colorado School Districts: An Overview of Selected Colorado Business Management Practices and Requirements.

INSTITUTION Colorado State Dept. of Education, Denver.

PUB DATE Jan 89

NOTE 25p.

PUB TYPE Guides - Non-Classroom Use (055)

EDRS PRICE MF01/PC01 Plus Postage.

DESCRIPTORS Accounting; *Budgeting; Business Administration; Compliance (Legal); *Educational Finance; Elementary Secondary Education; Financial Audits; *Financial Policy; Legal Responsibility; Long Range Planning; Money Management; Program Budgeting; Public Policy; Recordkeeping; Records (Forms); Resource Allocation; School Business Relationship; School Districts; *State Legislation

IDENTIFIERS *Colorado

ABSTRACT

Guidelines to help school district supervisors and business management personnel implement state-required financial policies and procedures are presented in this report. Steps to comply with Colorado regulations for budgeting, accounting, reporting, and auditing processes are discussed. Figures illustrate the budgeting cycle and schedule. (LMI)

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BUSINESS MANAGEMENT

PRACTICES
AND
REQUIREMENTS

FOR COLORADO SCHOOL DISTRICTS

An Overview of Selected
Colorado
School Business Management Practices
and
Requirements

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January 1989

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AN OVERVIEW OF SELECTED COLORADO SCHOOL BUSINESS MANAGEMENT PRACTICES AND REQUIREMENTS

Introduction

Recognizing Business Management Responsibilities and Planning to Perform Business Management Duties

This publication is designed to help superintendents and business management personnel establish and implement policies and procedures which Colorado school districts must follow in budgeting, accounting, reporting, and auditing. It is also hoped that new board of education members and others interested in the financial management of schools will profit from a review of this material. The contents of this overview serve as an easy-to-understand reference.

Other more detailed publications will be helpful in building a complete understanding of business management issues. These include the most recent version of the Financial Policies and Procedures (FPP) Handbook and the Annual Budget Workshop Manual. All districts should have copies of these publications. If these are not available in your district, please call the Colorado Department of Education (CDE) School Finance Unit for assistance. An additional reference is the U.S. Department of Education Handbook II, Revised, which is titled Financial Accounting, Classification and Standard Terminology for Local and State School Systems 1973 published by the National Center for Educational Statistics. While this federal publication is now out of print, if you wish to acquire a copy of Handbook II, Revised, please call the School Finance Unit. In addition to these basic references, school districts should also possess copies of updated Colorado revised statutes and State Board of Education rules as well as Colorado

Department of Education audit guides used for district audits conducted by the Department.

General Budgeting Strategies

The purpose of a budget is to provide a plan of financial operation embodying an estimate of proposed expenditures for a given period and purpose and the proposed means of financing that plan. To achieve this basic purpose, a comprehensive budget system must be integrated with the financial accounting system. Primary budget objectives provide:

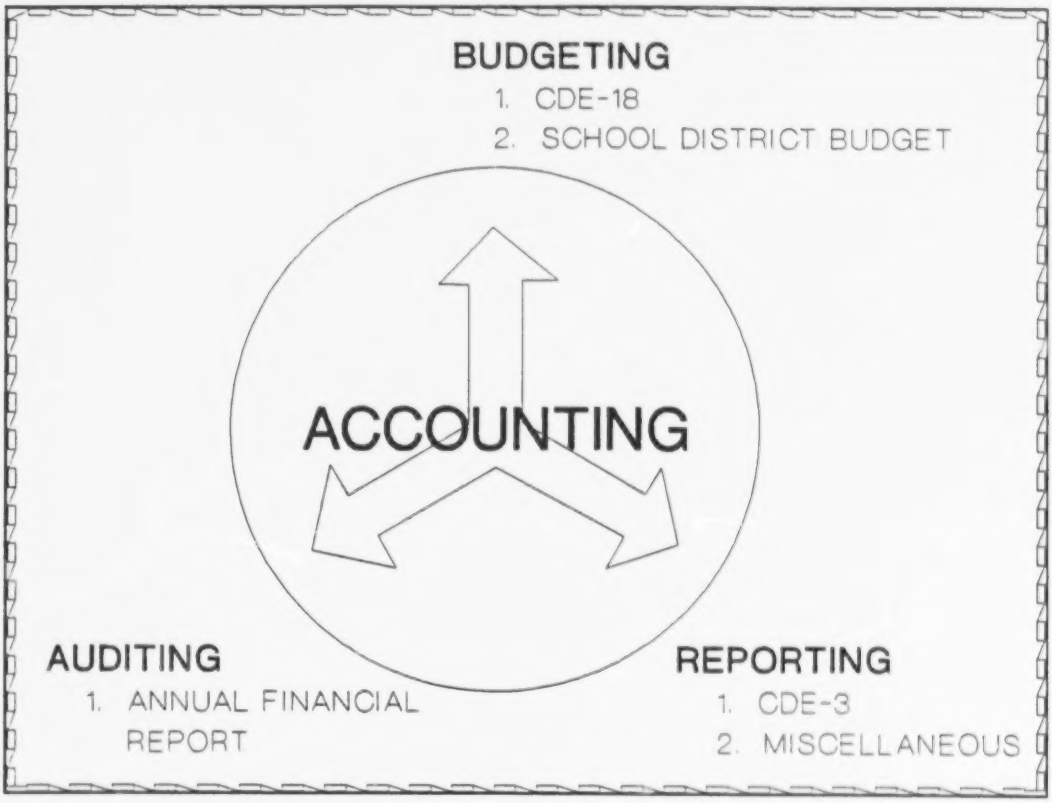
- A framework to assist in the formulation of an integrated plan of operations and in the understanding of how each program's activities contribute to the goals and educational needs.

- A means of communication through the budget process to school district staff and community by stating the objectives of each program and the funds necessary to achieve them.

- A means for relating anticipated costs and actual costs to designated programs.

- The historical data required for realistic budget preparation and related planning decisions, and practice consistent budgeting and reporting.

School fiscal management services are characterized by a cycle of Budgeting, Auditing, and Reporting activities. These three activities are all supported by Accounting. This relationship is shown in the figure below:



The Budget Cycle

A simplified time-line chart representing the chronology of the Budget Cycle is shown in the figure below. This diagram also illustrates some of the relationships between activities.

Budget Cycle Activities Time-Line

	Budget	Reporting	Auditing
January		Annual budget summary due	Preparation of year-ended financial statements; independent auditor conducts audit for prior year
February	Preparation of following year's budget (ongoing)		
March			Previous independent audit completed
April	Ongoing review of current budget (Analysis for following year)	Monthly report of district financial condition to board	Periodic financial reports (throughout the year)
May			Review of Audit to assist in planning for current year audit (and for following year budget preparation)
June			
July		Audit submitted to state	
August	CDE Budget Workshops including revenue projections	Annual transportation reimbursement report	
September	Proposed budget to local board of education		Contract for independent audit
October	Advertisement of budget to community	Annual pupil count and report to state for following year funding	
November	Revision of proposed budget		Prepare to complete financial statements with any necessary changes from previous year
December	Adopt budget		

Budget Preparation

Usually budget preparation is one of the major projects a superintendent or business manager must complete. The budgeting process calls for an examination of current accounts as well as an answer to the question, "Are we on schedule for revenues and expenditures in the current budget?" It is important to perform budget monitoring, control, and analysis functions to insure that district budgets are on target and to provide revised estimates of ending balances to forecast future financial situations.

Accurate accounting records must be maintained so that reporting and budgeting activities can be completed. Accounts are identified for each school district fund, including the General Fund, Capital Reserve Fund, Insurance Reserve Fund, Bond Redemption Fund, Pupil Activity Fund, and Food Service Fund. These funds are defined in the Financial Policies and Procedures (FPP) Handbook.

Budgeting is a complex activity which requires a clear picture of revenues and expenditures for each fund. Accounts are used to designate sources of revenue and purposes for which expenditures were made. Suggested account code organization and codes for the designation of revenues and expenditures are included in the Chart of Accounts section of the FPP Handbook. A discussion of the rationale for and design of account codes is found in the Account section of Handbook II Revised.

Why is a Budget Prepared and What is Required in a Proposed Budget?

The purpose of a budget is to provide a plan of financial operation including an estimate of proposed expenditures for a given period and purpose and the proposed means of financing that plan. To achieve this basic purpose, a comprehensive budget system must be integrated with the financial accounting system.

Detailed budget planning allows a district to reflect educational values and needs. The structure and format provided by a well-designed budget promotes rational decision making regarding the importance of various school district services. In this way, administrators and boards of education are assisted in educational planning as well as in the prioritization and planning of all district operations through the allocation of resources.

Budgets are also prepared to meet statutory requirements which assure school district fiscal accountability to the community and to the state (Colorado Revised Statutes 22-44). More detailed information on these requirements is found in the Budget section of the FPP Handbook.

To meet statutory requirements, the proposed budget must meet four basic tests. These tests are framed as questions below.

1. Is a separate budget prepared for each fund of the school district?
2. Does each fund budget show a comparison of revenues and expenditures amounts for three years (prior year, current year, ensuing year)?
3. Does each fund budget show revenues, expenditures, beginning fund balance, and appropriation amounts?
4. Are educational and other management goals to be realized through application of the budget specified in the proposed budget?

If all of these questions are answered "Yes," the school district is probably meeting statutory requirements. If each of these requirements is met and sufficient detail is provided, the proposed budget will be useful as a guide to decision making and planning. The following is a detailed review of each of these questions.

Criteria for a Legal and Useful Proposed Budget

1. The proposed budget is to represent all of a school district's activities. Therefore, a separate budget detailing revenue and expenditures must be prepared for each fund. This is required by law. Many districts will fulfill this requirement by preparing a budget for the General Fund, Capital Reserve Fund, Bond Redemption Fund, Pupil Activity Fund, Insurance Reserve Fund, and Food Service Fund. Others will also prepare a budget for Governmental Designated-Purpose Grants Funds, Trust and Agency Funds, and Other Enterprise Funds.

REMEMBER, a separate budget detailing revenues and expenditures must be prepared for each fund and an appropriation resolution must be made for each fund!

2. The fiscal year for school districts in Colorado is the calendar year. For each fund the budget must show a comparison of revenues and expenditures for three different years. If a budget for the 1989 calendar year is being prepared, a comparison of actual amounts for 1987, amounts from the budget adopted for 1988, and proposed budget amounts for 1989 must be shown. Administrators may also wish to show estimated projections for 1988 along with the 1988 budget amounts. These comparisons are usually made in a columnar format. Each year, the Budget Workshop Manual contains a printout which shows actual and budgeted General Fund revenues and expenditures for the two years prior to the year for which a budget is being developed. The printout shows expenditures by function and object codes presented in the Chart of Accounts section of the FPP

Handbook. With the addition of proposed amounts for the ensuing year, the basic three-year requirement described here will be met.

3. For each fund, minimum requirements regarding transactions and amounts to be shown are as follows: Each fund budget should show

    a) Projected beginning fund balance

    b) The projected revenues by source

    c) The projected expenditures within recommended account definitions

    d) The total amount to be appropriated for each fund

By law, a district may not spend more than the appropriated amount for each fund. A prepared appropriation resolution page is provided in the Annual School District Budget Summary (CDE-18). Unless a district has elected to keep a nonappropriated reserve (which cannot be spent during the year for which the budget is proposed), all fund appropriations should match budgeted revenues and expenditures.

4. By law, C.R.S. 22-44-108, a statement shall be submitted with the proposed budget describing the major objectives of the educational program to be undertaken by the school district during the ensuing fiscal year. This statement is also used to describe the manner in which the budget proposes to fulfill such objectives.

5. Beginning with the 1989 budget year, the district must budget a minimum amount within two specific accounts of the General Fund. These two accounts are referred to as the Instructional Supplies and Materials Account (Function 1000, Object 400) and the Instructional Capital Outlay Account (Function 1000, Object 500). Within these two accounts, the district must budget a minimum $110 per pupil based on the October 1 Funded Pupil Count preceding the budget year.

More Information About Budgeting and Budget Strategy

Budgets are based on anticipated circumstances of district needs and projected revenues. Changes in these circumstances can occur. Prudent budget practices include building some flexibility into the district budget and being aware of legal options in budget implementation. Some of these strategies and options are listed below.

Reserves for Contingencies. In Colorado, property tax and state equalization shortfalls have occurred frequently in recent years. The likelihood of property tax shortfalls varies by district, but all districts are affected when a recision based on state revenue shortfalls occurs. When these kinds of reductions in projected revenues are likely, wise business management practices dictate establishing reserves for shortfalls in the operating budget. If no shortfall occurs, this reserve will be available for use. However, if shortfalls do occur, the integrity of budgeted expenditures within a fund will not be compromised. In addition contingency funds are used if other revenue categories are not realized or if expenditures are greater than program budgets.

Transfers. Beginning with the 1989 budget year, the district must transfer from the General Fund a minimum of $200 per pupil to the Capital Reserve Fund and/or the Insurance Reserve Fund for expenditures as described in C.R.S. 22-53-108(3)(c). The district may transfer up to $800 per pupil. The number of pupils is established by the October 1 Funded Pupil Count preceding the budget year. The district may transfer, upon need, funds between the Capital Reserve Fund and the Insurance Reserve Fund subject to the provisions of C.R.S. 22-44-112.

Borrowing. Occasionally, districts find it necessary to accommodate short-term revenue shortfalls by borrowing between funds or from banks. Interfund borrowing can involve any fund except the Bond Redemption Fund and requires a board resolution. Amounts between funds must be repaid within the first three months of the following year. Districts may engage in short-term borrowing from banks. The amount and interest rate of such loans are limited by law and the loans must be repaid within six months. Statutory citations and more information can be found in the Audit section of the FPP Handbook.

Supplemental Budgets. When districts receive unexpected revenues for a specific purpose from sources other than ad valorem taxes, a supplemental budget and appropriation may be adopted. This budget must be adopted and appropriations made by the board of education before such funds are spent. There is no requirement that a supplemental budget be reported to the state. However, a copy of the supplemental budget should be provided to independent auditors. One example of this kind of circumstance might be receipt of unexpected governmental designated-purpose grants.

Budget Publication. An additional legal requirement is that the board of education shall cause to be published a notice stating that the proposed budget is on file and when the board will consider adoption of the proposed budget.

An Overview of Accounting Organization

An examination of budgeting, reporting, and auditing activities shows the need for effective school district financial accounting as a basis for all of these efforts. The importance of accounting justifies the extensive planning and publication of materials dedicated to this subject. School districts have access to several different guides relating to installation and maintenance of an accounting system.

Accounting organization is addressed in the FPP Handbook which also describes Generally Accepted Accounting Principles (GAAP) for school districts and provides code definitions for nearly all applications of school district reserve. The Handbook is designed so that various fund definitions (General Fund, Bond Redemption Fund, Capital Reserve Fund, Insurance Reserve Fund, Enterprise Fund [Food Service, and others], and special purpose funds) are provided. Coding for different sources of revenues includes tax collections, state grants-in-aid, fees and other charges, interest earned, etc.

Account coding for expenditures is also provided in the FPP Handbook. Expenditure coding is much more detailed than that for revenue. This is because school districts direct funds for many different purposes within each fund. It is important for educational planning and budgeting to determine for what purposes funds have been spent and to reconcile these expenditures. For these reasons, a number of different expenditure codes are available.

The minimum required reporting account codes for district expenditures are referred to as Function and Object codes. Function codes describe the purpose for which expenditures were made. Examples of function codes include 1000 (instruction), 2100 (pupil support services), 2400 (school administration), and 2550 (pupil transportation). Object codes describe the service or commodity obtained as the result of a particular expenditure. Examples of object codes include 100 (salaries), 200 (benefits), 300 (purchased services), 400 (supplies and materials), 500 (capital outlay), 600 (other expenses), and 700 (transfers).

Each of these and other functions and objects are assigned a numerical code in order to facilitate computerized accounting system design. Each function and object code can be extended with recommended numerical information in order to further define expenditures. As an example, function 1000 denotes instructional expenditures, function code 1100 denotes Regular Programs, function code 1110 represents Regular Elementary Instruction, 1120 Regular Middle Level Instruction, and 1130 Regular High School Instruction. Similar extended detail is provided for object definition as well. For example, salaries are reported under object 100 with object 110 denoting regular salaries, 120 temporary salaries, and 130 overtime salaries. Refer to the FPP Handbook Chart of Accounts section.

In addition to these basic expenditure account codes, the FPP Handbook provides additional code definitions which allow a district to break down revenues and expenditures in greater detail. School districts are encouraged to expand account codes to differentiate between expenditures for locally defined programs such as language arts, science, and math, as well as between different locations (school buildings) and activities involved in provision of instructional services.

The Connection Between Reporting and Accounting

Each school district in Colorado should prepare and have audited, a general purpose financial statement that includes all funds and activities of the district, and the general fixed asset account group. The requirement for annual financial statements in conformity with Generally Accepted Accounting Principles (GAAP) is set forth in the Colorado Local Government Audit Law. Complete annual financial statements covering all funds and activities, including appropriate combined, combining, and individual fund statements, must be prepared, audited, and submitted to the State Auditor no later than July 31 of each year. Financial statements must include a comparison of budgeted amount to actual for all funds and activities. In addition, the Annual School District Financial Report (CDE-3) must be included in the audit schedule.

The annual financial statements should be prepared in accordance with GAAP. The combining and individual fund schedules must be prepared in accordance with the formats prescribed by the Colorado Department of Education. All schedules must be bound into one report.

Periodic reports are used to analyze the current financial status of a district and in projecting year-end financial status. Districts must be able to recover accurate financial information on a timely basis. The reporting requirement demands that an organized accounting system be installed and maintained.

It has been noted that both revenues and expenditures are accounted for by fund and that guidelines for account definition are provided in the Handbook II, Revised, and presented, in part, in the FPP Handbook. Success in applying account codes as a source of accounting organization determines the extent to which accurate reports can be provided AT LEAST by Fund, Function, and Object. See the Accounting section of FPP

Handbook for more information.

All phases of reporting are facilitated when accounts are well defined and information is quickly retrievable. The use of regular reports to monitor budget implementation makes preparation of next year's budget easier. Adequate account organization allows comparison of revenues received in each fund to revenues expected during that period. Similar comparisons can be made for each expenditure account. With this information in hand, district financial management can proceed from an informed perspective and preparations for adjustments, either in the current year expenditures or in the following year's budget, can be made.

Internal Reporting

The main objective of internal financial reporting is to inform each management level in the district of current budget implementation and status. Levels to be informed are:

1. Board of Education
2. Central Administration
3. Building Administration

For the board of education, periodic reports are required. These reports show the current status of revenues and expenditures in the various funds. A comparison of revenues and expenditures to date with budgeted amounts for each fund and expenditure category should be provided. With this information the board can review and respond to developing trends.

The reports provided to the board of education also may be used as an informative tool for district administration. Usually, however, this general data needs to be broken down further to show the budget status of individual departments, organizational units, or programs within the district. In small districts this might not be necessary. Where required, the emphasis is on data comparing total expenditures to date, month-by-month expenditures, and remaining balances adjusted to reflect changes, if any, in the revenue picture of the district.

The same general approach may be used for building level reporting. Here the building budget status should be provided as well as information regarding the status of each program budget within the building. The objective is to determine if the adopted budget is being followed and to assist administrators and other staff members to determine where adjustments are needed.

External Reporting

Reporting Financial Data to Colorado Department of Education

School districts are required by statute to report financial data to the state and to other agencies or organizations for a number of different purposes. Also, districts must submit additional data and related information to the state to receive benefits under school support laws.

All districts are responsible for two major reports of financial data to the state. These are the Annual School District Budget Summary (CDE-18) and the Annual School District Financial Report (CDE-3).

The CDE-18 is not designed to be a proposed budget and cannot serve as a district's budget. The CDE-18 budget summary form does not, for instance, provide

the mandatory three-year comparison of revenues and expenditures. Instead, form CDE-18 provides a format for reporting beginning fund balance, projected revenues, and budgeted expenditures for selected funds of a school district.

These are the General Fund, Capital Reserve Fund, Insurance Reserve Fund, and Bond Redemption Fund. A place to show total budgeted expenditures for Governmental Designated- Purpose Grant Programs when treated as a separate fund or funds is also provided. Finally, a resolution page provides a place where appropriated amounts for each of a district's funds are entered along with a sample resolution for Board action in adopting the budget. The CDE-18 is distributed in the early fall and must be submitted to the School Finance Unit by January 30. CDE-18 data is used for state level analysis, reporting to the Colorado General Assembly and for federal reports.

Information is also required in order to determine district entitlement under the Public School Finance Act, the Public School Transportation Fund, the Exceptional Children's Educational Act, and others. Districts may elect to recover indirect costs for managing federal programs and the calculation of the required rates may require submission of additional data to that provided in the CDE-3 report.

Other External Reporting

School districts also prepare and submit financial reports for other reasons. For example, year-end financial statements and the audit report are available for public examination. These are examples only and not a comprehensive list. Districts also must prepare reports to the federal government. Federal reports include those made to report wages and tax withholding. Reports are also required for educational programs which are funded, in part, with federal funds. When districts issue bonds for building purposes,

financial reports are usually submitted to bond rating agencies and, in some cases, to investors. To qualify for federal lunch program support, districts must submit complete financial reports to the state agency (CDE) which regulates disbursement of those funds.

The Connection Between Auditing and Accounting

Annual independent audits of each school district's financial reports and accounting practices are required by both state and federal law. In addition, the independent audit can and should serve as a means for each district to evaluate and improve its business management system.

Independent financial audits serve as tools for administrators and board of education members to confirm the financial condition of the district and to publicize this information to the public. At the same time, the auditor has an opportunity to recommend changes in accounting and reporting practices. To realize the benefits of proper independent audits, to assure compliance with statutes and regulations, and to make the audit process run smoothly, it is important for administrators to understand audit procedures and requirements. The Audit section of the FPP Handbook provides information regarding statutes and regulations and a sample request for proposal which districts can use to solicit independent audit bids. In addition, an audit checklist is provided. This checklist can be used to review district and auditor responsibilities with the district auditor.

Preparation of accurate financial statements requires an organized accounting system. Without means to code and identify revenues and expenditures by fund and use, a district is unable to prepare accurate financial statements. Audited financial statements must conform to Generally Accepted Accounting Principles (GAAP) for

government entities and use of recommended account definitions provides a basis for compliance with this requirement (refer to FPP Handbook).

In addition to reviewing the financial statements of a school district, independent auditors must attest to the fact that the reports represent the true financial condition of the district. Accounting procedures require an "audit trail" for each transaction. Developing a useful audit trail involves establishing authority for making expenditures, and being able to determine the amount, timing, and fund for revenues received. Detailed accounting codes, as recommended in the Chart of Accounts section of the FPP Handbook, provide a basis for this accounting. Use of appropriate account codes allows a district to report accurately revenues and expenditures. Accounts definition also expedites preparing a summary of data for all types of financial reports.

Auditing

All school districts are required by state law to have annual independent financial audits. Most districts must also comply with the "Single Audit Act of 1984" (a federal requirement).

Independent auditors examine the financial statement of all funds and account groups. Then they assess whether or not the statements fairly represent the financial position and results of operations of a school district in conformity with GAAP. In connection with the audit, the auditor may recommend improvement in financial management and internal control procedures. If a weakness is detected, the auditor is required to report this to the proper level of administration. The auditor should review the audit report and recommendations, if any, with the local board of education. This review is conducted to provide the board an opportunity to understand audit findings and

recommendations.

The audit process and report serves as a review of financial management and internal control. It helps districts to meet statutory requirements, account to the public, and provide for efficient, traceable use of school funds.

Preparing for the Audit

The district should prepare in advance for the audit. This will not only simplify the auditor's work, but will save the district money. Since the auditor is paid according to the scope of the job, preliminary work done by the district is cost efficient. Before an audit estimate is requested, determine what work will be prepared by the district and what work will be completed by the auditors. Some examples of schedules and worksheets which might be prepared by the district prior to the audit include:

1. Trial Balances
2. Bank Reconciliations
3. Confirmations
4. Inventory Schedules

Auditing Responsibilities

School districts are ultimately responsible for preparing financial statements which conform to Generally Accepted Accounting Principles (GAAP), comply with state and federal audit requirements, and for compliance with statutes or regulations related to the use of funds. These requirements include limitations on the type of expenditures to be made from each of the funds and are largely designed to preclude misuse of funds by local boards of education. If an auditor finds that GAAP or statutory requirements have

not been followed, this information will be reported to the board. In addition, audits will be reviewed and the auditor's findings examined by the State Auditor's Office and by the Colorado Department of Education. These units will then communicate any problems and required solutions to the local board of education.

The requirement for audit completion and submission is defined by state law. Independent auditors are required to submit a completed report of the audit to the school district within six months after the end of the calendar year. The district or the auditor is then required to submit copies of the audit to the State Auditor's office and to the Department of Education within 30 days of the report to the district. Most districts are also required to submit a copy of federally funded program audits to a national clearinghouse.

Conclusion

This publication is designed with the superintendent and business management personnel in mind. Our goal is to help establish and implement policies and procedures which Colorado school districts must follow in budgeting, accounting, reporting and, auditing. Board members and other interested persons will profit by the review of this material. To attain a more indepth understanding of business management issues, we recommend the most recent version of the Financial Policies and Procedures (FPP) Handbook, published by the Colorado Department of Education School Finance Unit.